

12 February 2021

Dr Kerry Schott  
Independent Chair  
Energy Security Board

*Sent electronically*



Dear Dr Schott,

### **Submission to Renewable Energy Zone second stage consultation paper**

The Public Interest Advocacy Centre (PIAC) is an independent, non-profit legal centre based in New South Wales. Established in 1982, PIAC tackles systemic issues that have a significant impact upon people who are marginalised and facing disadvantage. We ensure basic rights are enjoyed across the community through litigation, public policy development, communication and training. The Energy + Water Consumers' Advocacy Program represents the interests of low-income and other residential consumers, developing policy and advocating in energy and water markets.

PIAC welcomes the opportunity to respond to the ESB's consultation paper on Renewable Energy Zones (REZ).

#### **The importance of delivering REZs**

REZs are an important tool to both accelerate emissions reductions and lower energy prices. The current issues with access, risk allocation and cost recovery that prevent the implementation of REZs are challenges that need to be addressed to help deliver REZs as efficiently as possible.

PIAC cannot support a solution that seeks to make only minor changes now and leaves solving the underlying issues that prevent REZs to the implementation of broader transmission access and pricing reforms. The AEMC's Coordination of Generation and Transmission Investment (COGATI) process has shown there is no clear consensus yet on how or when to implement these broader access reforms. Waiting for this consensus to be developed and then implemented is too slow to deliver REZs.

#### **Principles for risk and cost**

Given the importance of REZ investment, it is essential the frameworks for delivering these are founded on strong principles to allocate risk and recover costs. Risks are most efficiently allocated to the parties that are best placed to manage them. Consumers are not able to manage any of the risks in either the transmission or generation investment necessary for a REZ and it is unacceptable they be expected to bear these entirely. Costs are best recovered from parties on a beneficiary-pays basis or, where that is impractical, on a causer-pays basis.

An essential component of any REZ framework must be that connecting parties should contribute to covering REZ costs if they receive some form of access rights. To do otherwise would breach the beneficiary-pays principle and send inefficient price signals.

PIAC does not consider there is any evidence or valid reason for connecting parties to reject this principle. As the ESB notes in its consultation paper, the economies of scale possible through a REZ means that connecting parties

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would likely pay less to connect within a REZ with some level of guaranteed or improved access rights than connecting elsewhere in the NEM.

### **PIAC's risk- and cost-sharing model**

PIAC welcomes the ESB considering the risk- and cost-sharing model for REZ funding we have shared previously through the COGATI and the Post-2025 Market Design processes. However we reject the ESB's assessment of it.

The ESB has stated PIAC's model would lead to increased complexity and this may be a reason to not pursue the model further. Addressing the underlying issues and delivering REZs in a timely manner are not straightforward problems, and simple solutions are unlikely to adequately solve them. Instead, any simple solution is likely to result in consumers bearing risks they cannot manage and inefficient cross-subsidisation between connecting parties. Therefore, complexity must not be used as an argument against implementing a workable solution.

The ESB also states that the generator and speculative investor costs could be passed through via the wholesale market. PIAC does not consider this to be a disadvantage of the model as these costs would only be passed through to consumers, through the functioning of a competitive market, if the costs themselves are efficient and the investment was prudent. This is actually an advantage over the status quo for regulated investments where these costs are passed through to consumers regardless. We note that this is also the case with the auction or tendering costs REZ generators would incur under the ESB's proposed model.

The issues highlighted by Project EnergyConnect show that strategic transmission investments are often inconsistent with the business model or risk appetite of incumbent transmission shareholders. Recent concerns regarding the financeability of REZs also highlights the importance of contestability in financing these projects, as through PIAC's model.

While alternative options exist to the PIAC model, these do not deliver the principles described earlier regarding risk allocation or cost recovery. They either result in unacceptably high risk and costs for consumers or unacceptably high risks for generators. Compared to the status quo, PIAC's model offers a more cost-effective way for generators to connect and lower risk.

PIAC recommends the ESB adopt the PIAC risk- and cost-sharing model for REZ financing to reduce the risk borne by consumers and better allocate these risks to parties that can manage them.

This is also described in our response to Question 12.

### **Impact of generators outside the REZ**

Any system-wide planning process that would drive the creation of a REZ, such as the ISP, should also consider any downstream impacts from existing network constraints and likely future connections. For instance, this could include reinforcement of an existing transmission line or the creation of a new line near where a REZ connects to the existing shared transmission network to increase the power transfer capacity to major load centres.

This approach is used in PIAC's risk- and cost-sharing model for REZs. A new generator outside the REZ but connecting to the downstream transmission investment necessary for the REZ would be liable to pay for their portion of it. This follows the principles of allocating risk to parties best placed to manage them and recovering costs on a beneficiary-pays basis.

**Continued engagement**

PIAC would welcome the opportunity to meet with the ESB and other stakeholders to discuss these issues in more depth.

Yours sincerely,

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## Responses to consultation questions

### **Question 1: Are REZs an appropriate interim solution to the challenges associated with open access?**

REZs are not an interim solution. Rather, REZs are an important tool to both accelerate emissions reductions and lower energy prices. The current issues with access, risk allocation and cost recovery are challenges that need to be addressed to help deliver REZs as efficiently as possible.

### **Question 3: Do stakeholders agree with the proposed objectives for a regulated REZ development model?**

PIAC agrees with the three proposed objectives.

In particular, we strongly support the objective to “reduce the level of risk and cost borne by customers.” PIAC’s cost and risk sharing model is designed specifically to achieve this by allocating risk and costs away from consumers and to parties better able to manage the risks and directly benefit from the investment. Reducing the consumer-borne costs by offsetting TUOS with the proceeds from the tendering or auctioning of REZ access rights is another important tool to help achieve this objective.

### **Question 5: Which party is best placed to perform the role of REZ coordinator where the REZ is being developed in accordance with the regulatory framework? Should the decision regarding the identity of the REZ coordinator lie with the State government?**

Another option for the REZ Coordinator is to create a Panel including AEMO, the AER and the TNSP. PIAC opposes the REZ Coordinator being the TNSP alone. This Panel could be formed at either a state-specific or national level.

PIAC considers it is appropriate that the decision of who to appoint as the REZ Coordinator sit with the state government.

### **Question 6: Are the functions to be undertaken by the REZ coordinator in the regulated model appropriate?**

Yes.

PIAC recommends the REZ Coordinator also have an advisory role in the design and staging decisions for both the network infrastructure and auctioning of access rights for a REZ.

### **Question 11: Should the REZ coordinator return any surplus auction proceeds to customers in the form of a reduction in TUOS charges?**

PIAC strongly supports all auction proceeds offsetting TUOS for consumers. Reducing the consumer-borne costs helps to minimise the risk borne by consumers. Instead, it transfers the risk to the connecting parties who are better placed to manage it and helps ensure costs are recovered on a beneficiary-pays basis.

However, we note that PIAC’s risk- and cost-sharing model would better achieve this by better allocating risks away from consumers from the outset.

**Question 12: Should the ESB consider REZ models that allow for speculative investment that departs from the ISP, in order to reallocate risk away from customers, such as the one put forward by the Public Interest Advocacy Centre (PIAC)?**

PIAC strongly supports this the use of the risk- and cost-sharing model for REZs.

The model is designed specifically to promote clear and efficient market signals by ensuring risks are borne by parties best placed to manage them and costs are recovered on a beneficiary-pays basis.

PIAC is concerned by the ESB's assessment that it would lead to increased complexity and disagree that this may be a reason to not pursue the model further. Addressing the underlying issues and delivering REZs in a timely manner are not straightforward problems, and simple solutions are unlikely to adequately solve them. Instead, any simple solution is likely to result in consumers bearing risks they cannot manage and inefficient cross-subsidisation between connecting parties. Therefore, complexity must not be used as an argument against implementing a workable solution.

PIAC also disagrees that the model's speculative investments would allow departures from the ISP in order to reallocate risk away from consumers and considers the ESB may have misunderstood this aspect of the model. Under the model, the risk-reallocation away from consumers is only for REZ capacity consistent with the ISP. The speculative amount is an opportunity for a contestable investor to offer capacity above and beyond what was determined in the ISP – this risk would be borne entirely by the investor and is not a reallocation away from consumers.

PIAC also rejects the ESB's assessment that the model creates a disincentive to invest in the REZ relative to the rest of the NEM and notes this statement is not substantiated in the consultation paper. As the ESB themselves note, the model better allocates stranding asset risk, supports meshed configurations, integrates market drivers with transmission planning and provides clarity up front regarding cost allocation. In addition to the general benefits of connecting to a REZ, PIAC considers the model would positively incentivise connection within a REZ relative to elsewhere in the NEM.

**Question 15: Are the evaluation criteria set out in the introduction to Chapter 5 appropriate?**

PIAC supports the evaluation criteria.

In particular, promoting efficient risk allocation is an important criteria to send appropriate signals to the relevant parties. As noted earlier, risk is most efficiently allocated to the parties best placed to manage it and costs are most efficiently recovered from beneficiaries. Therefore, connecting parties should contribute to covering REZ costs if they are to receive some form of access rights.

**Question 16: Which option for access within a REZ is preferable?**

Of the options presented in the paper, PIAC considers the financial access protection model the most appropriate.

PIAC does not support the early allocation of financial transmission rights (FTR) as a viable solution. In order to be effective, this option would require a clear vision of how and when locational pricing and FTRs would be implemented across the NEM. There does not appear to

be the necessary consensus yet and waiting for one to develop and then be implemented will be too slow to deliver the REZs necessary to reduce emissions and energy bills.

**Question 18: Are there potential improvements to the options that the ESB should consider?**

See response to Question 19.

**Question 19: If the ESB were to adopt one of the access options outlined in this chapter, would it be necessary to restrict connections outside of REZs?**

Some of the issues from the impact of generators connecting outside of a REZ can be addressed by extending the REZ framework (including cost recovery and access rights) beyond only the new transmission investment from a REZ reference node. Instead, it could also apply to any upgrades or reinforcements necessary to the downstream transmission network in order to optimise congestion between the generators in a REZ and major load centres.

Any system-wide planning that identifies and drives the development of a REZ, such as the ISP, should also consider any upstream impacts from existing network constraints and likely future connections. For instance, this could include reinforcing an existing transmission line near where a REZ connects to the existing shared transmission network in order to increase the power transfer capacity.

This approach is used in PIAC's risk- and cost-sharing model for REZs. A new generator outside the REZ but connecting to the downstream transmission investment necessary for the REZ would be liable to pay for their portion of it. This follows the principles of allocating risk to parties best placed to manage them and recovering costs on a beneficiary-pays basis.